

IT 02-5

Tax Type: Income Tax

Issue: Reasonable Cause on Application of Penalties

**STATE OF ILLINOIS
DEPARTMENT OF REVENUE
OFFICE OF ADMINISTRATIVE HEARINGS
CHICAGO, ILLINOIS**

**THE DEPARTMENT OF REVENUE
OF THE STATE OF ILLINOIS**

v.

ABC CONSTRUCTION, INC.,

Taxpayer

No. 01-IT-0000
FEIN: 00-0000000
TYE: 12/31/99

RECOMMENDATION FOR DISPOSITION

Appearances: Joseph P. Levon, Esq. on behalf of ABC Construction, Inc; Rickey A. Walton, Special Assistant Attorney General on behalf of the Illinois Department of Revenue.

SYNOPSIS:

This matter arose following the protest of a Notice of Deficiency ("NOD") issued by the Illinois Department of Revenue ("Department") on February 16, 2000 to ABC Construction, Inc. ("taxpayer") for the tax period of 1/Q/99 through 4/Q/99. Taxpayer paid its withholding tax on a monthly basis during this period. The Department issued the NOD and assessed penalties under Section 3-3(b-5) of the Uniform Penalty and Interest Act ("UPIA")¹ for failure to pay over

¹ 35 ILCS 735/3-3(b-5)

withholding tax on a quarter monthly basis as required under Section 704(b) of the Illinois Income Tax Act ("IITA")². At hearing, taxpayer presented evidence to support its request for an abatement of penalties due to reasonable cause. After reviewing this evidence, it is my recommendation that the penalties be abated.

FINDINGS OF FACT:

1. The Department established its *prima facie* case, inclusive of all jurisdictional elements, by the admission of the Notice of Deficiency dated February 16, 2001 for penalties assessed for the tax period 1/Q/99 through 4/Q/99. Dept. Ex. No. 1.
2. ABC Construction Inc. is a mason subcontractor. Tr. p. 10. The company has approximately 109 employees. Tr. p. 10.
3. John Doe is the president of ABC Construction. Tr. p. 10. Doe is responsible for remitting ABC's payroll taxes to the Department. Tr. p. 11.
4. Prior to the tax period at issue, ABC timely paid its taxes on a monthly basis. Tr. p. 14.
5. Doe received a letter from the Department in February of 2000 that requested information as to the taxpayer's withholding account. Upon receipt, Doe faxed it to the company's outside C.P.A., and requested that the C.P.A. contact the Department to inquire about the matter and send the Department the worksheets requested. Tr. pp. 14, 15.
6. The taxpayer began making timely quarter monthly payments of its withholding tax liabilities once advised to do so by the Department in May of 2000. Tr. pp. 21-22.

² 35 ILCS 5/704(b).

CONCLUSIONS OF LAW:

Taxpayer's responsibility for Illinois withholding tax is found in article 7 of the Illinois Income Tax Act. 35 **ILCS** 5/701 *et seq.* The time by which an employer must pay its withholding tax liabilities is governed by Section 704. Specifically, Section 704(b) provides that if the aggregate amount of wages deducted and withheld by the employer exceeds \$1,000 for a quarter monthly period, payments of those withholdings must be made quarter monthly. Section 704(c) provides that if withholdings for a month are between \$500 and \$1,000 then payment of the withholdings to the State are to be made monthly.

Prior to the first quarter of 1999, the taxpayer was correctly filing and paying its withholding liabilities on a monthly basis. It was only in January of 1999 that the company's payroll increased so that its increased employee withholdings placed taxpayer above the \$1,000 threshold outlined in Section 704 and required it to pay over withholding tax on a quarter monthly basis. Despite such, taxpayer continued remitting its full withholding tax payments on a monthly basis. It is clear from the record, however, that once taxpayer was advised by the Department that it was required to remit its withholding tax payments quarter monthly, it immediately corrected its procedures to comply and thereafter has timely paid on a quarter monthly basis.

The Department assessed penalties pursuant to Section 3-3(b-5) of the UPIA, 35 **ILCS** 735/3-1 *et seq.*, which provides for a penalty of 20% of the tax required to be shown due on a return for failure to pay the tax on or before the due date prescribed for payment. Taxpayer protested the Notice of Deficiency for the tax year ending December 31, 1999 alleging that the Section 3-3(b-5)

penalties assessed against it should be abated due to reasonable cause under Section 3-8 of the UPIA, 35 **ILCS** 735/3-8.

A determination as to whether reasonable cause exists must be made on a case by case basis taking into account all of the facts and circumstances. 86 Admin. Code ch. I, Sec. 700.400(b). Section 700.400(b) indicates that it must be determined to what extent the taxpayer made a good faith effort to determine the correct tax liability and to file and pay his proper liability in a timely fashion and subsection (c) provides that a taxpayer is considered to have made a good faith effort if he uses ordinary business care and prudence. Factors which are considered in determining whether the taxpayer exercised ordinary business care and prudence are the clarity of the law and its interpretation, and the taxpayer's education, experience and knowledge. *Id.* Depending on the facts and circumstances of the case, reliance on the advice of a tax professional may or may not establish that taxpayer exercised ordinary business care and prudence and justify an abatement of penalty. 86 Ill. Admin. Code ch. I, sec. 700.400(c). The regulation also provides that the taxpayer's filing history may be considered in determining whether the taxpayer acted in good faith in determining and paying his tax liability.

It is clear that taxpayer was required to pay its withholding taxes to the Department on a quarter monthly basis. However, it is undisputed from the record that the taxpayer's history of payment of these taxes is excellent prior to the tax period at issue. It is also undisputed that once advised of the requirement to pay quarter monthly, taxpayer did so immediately. Although taxpayer handled its payroll and its withholding tax filings internally with the help of a payroll service, as soon as the Department communicated concerns about its tax payments, the taxpayer contacted its C.P.A. and took immediate steps to file quarter monthly. Lastly, there is no evidence of record, that taxpayer has filed its quarter monthly payments late since the tax period at issue. Thus,

after reviewing the record in this matter and considering it in its totality, it is my recommendation that the penalties should be abated due to reasonable cause.

Wherefore, it is my recommendation that the penalties be abated due to reasonable cause and the Notice of Deficiency issued by the Department should be cancelled.

Date: February 21, 2002

Christine O'Donoghue

Administrative Law Judge